North Devon Council

Report Date: 3rd February 2025

Topic: Treasury Management Strategy Statement 2025/26

Report by: Adam Tape, Head of Governance

1 Introduction

This report sets out the Council's strategy for Treasury Management, Minimum Revenue Provision (MRP) and Investments for the forthcoming financial year.

2 Recommendations

The Committee is asked to recommend to full Council that:

2.1 The Treasury Management Strategy Statement, Minimum Revenue Provision Policy Statement and Annual Investment Statement 2025/26, including the Treasury Management and Prudential Indicators for 2025/26 to 2027/28, be approved.

3 Reasons for Recommendations

3.1 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (SI 2003/3146) requires the Council to have regard to the Treasury Management Code.

3.2 Under section 3(5) of the Local Government Act 2003 the Council is required to have regard to the Prudential Code when setting limits to the level of its affordable borrowing.

3.3 This Council is also required under the Code to give prior scrutiny of the treasury management reports by the Policy Development Committee before they are reported to the full Council.

4 Treasury Management

4.1 Background

Part of the treasury management operation is to ensure that cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

CIPFA defines treasury management as:

"The management of the local authority's borrowing, investments and cash flows, including its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day-to-day treasury management activities.

4.2. Reporting Requirements

The Council will receive and approve three main reports each year, which incorporate a variety of polices, estimates and actuals.

a) Prudential and treasury indicators and treasury strategy (this report) - The first, and most important report is forward looking and covers:

- the capital plans (including prudential indicators);
- a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

b) A mid-year treasury management report – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c) An annual treasury report – This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

These reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Policy Development Committee.

In addition to the three major reports detailed above, quarterly reporting (end of June / End of December) will also be required. These reports will include the updated Treasury/Prudential Indicators and this will be incorporated into the current Performance and Financial Management Reports to Strategy and Resources, Policy Development Committee and Full Council.

4.3 Treasury Management Strategy for 2025/26

The strategy for 2025/26 covers two main areas:

Capital Issues

- the capital expenditure plans and the associated prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury management Issues

- the current treasury position;
- treasury indicators which will limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- the policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, DLUHC (now MHCLG) Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

4.4 Training

The CIPFA Code requires the Chief Finance Officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.

Furthermore, the Code states that they expect all organisations to have a formal and comprehensive knowledge and skills or training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance and decision making.

The scale and nature of this will depend on the size and complexity of the organisation's treasury management needs. Organisations should consider how to assess whether treasury management staff and board/council members have the required knowledge and skills to undertake their roles and whether they have been able to maintain those skills and keep them up to date.

Treasury Management training was provided to Members after the district elections in May 2023 and will be refreshed during 2025. The training needs of treasury management officers are periodically reviewed.

1.5 Treasury Management Consultants

The Council uses MUFG Corporate Markets Treasury Limited (previously named Link Group) as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers. All decisions will be undertaken with regards to all the available information, including, but solely, our treasury advisors.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

5 The Capital Prudential Indicators 2025/26 – 2027/28

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

5.1 Capital Expenditure and financing

This prudential Indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts:

Capital Expenditure £000	2023/24 Actual	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
Customer Focus	208	226	70	*350	*350
Environmental Enhancement	430	4.484	314	0	0
Governance	0	0	0	0	0
Place & Regeneration	5,300	9,449	10,756	*490	*830
Planning, Housing & Health	4,208	6,031	3,299	1,212	*1000
Total	**10,146**	**20,190**	**14,439**	**2,052**	**2,180**

** Estimates as PAG bids not yet approved by Members*

The above financing need excludes other long-term liabilities, such as the finance lease arrangements for our vehicle fleet as they already include borrowing instruments.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Financing of Capital Expenditure £000	2023/24 Actual	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
Capital receipts	(277)	(320)	(150)	(150)	(80)
Capital grants	(7,400)	(11,772)	(6,563)	(1,212)	(1,000)
Capital reserves	(1,026)	(1,352)	(632)	(315)	(215)
Net financing need for the year	**1,443**	**6,746**	**7,094**	**375**	**885**

5.2 The Council’s Borrowing Need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so it's underlying borrowing need. Any capital expenditure in the table above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each assets life, and so charges the economic consumption of capital assets as they are used.

The CFR includes any other long-term liabilities (e.g., PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility by the PFI, PPP lease provider and so the Council is not required to separately borrow for these schemes. The Council currently has circa £5.3m of such leases within the CFR.

The Council is asked to approve the CFR projections below:

£000	**2023/24 Actual**	**2024/25 Estimate**	**2025/26 Estimate**	**2026/27 Estimate**	**2027/28 Estimate**
Capital Financing Requirement					
Total CFR	**26,044**	**34,549**	**40,549**	**40,103**	**39,620**
Movement in CFR	**2,178**	**8,505**	**6,000**	**(446)**	**(483)**

Movement in CFR represented by:					
Net financing need for the year (above)	1.443	6,746	7,094	375	885
Financing Lease – Capital Costs	1,627	2,864	284	865	500
Less MRP	(741)	(784)	(812)	(1,047)	(1,089)
Finance Lease Principal Payments (MRP)	(151)	(321)	(566)	(639)	(779)
Movement in CFR	**2,178**	**8,505**	**6,000**	**(446)**	**(483)**

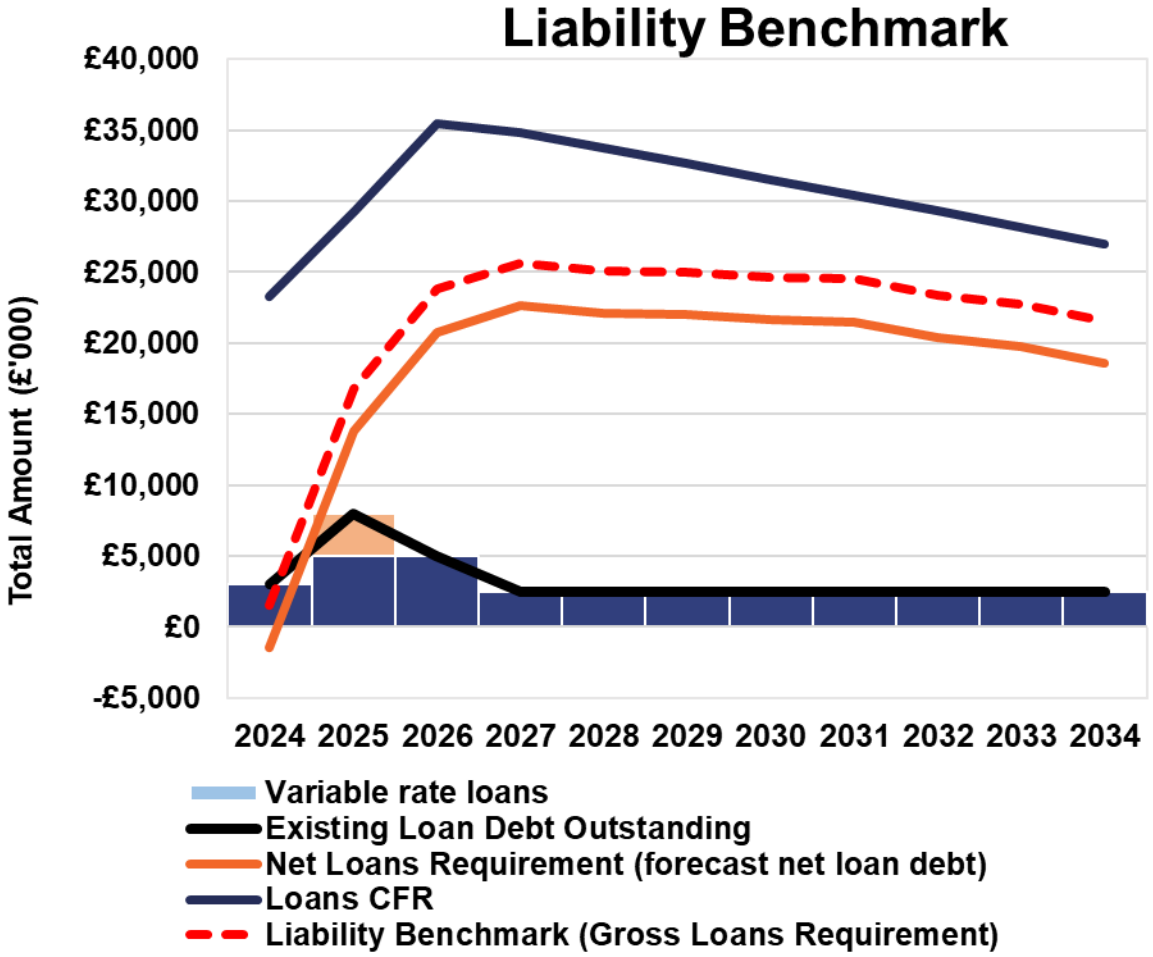
5.3 Liability Benchmark

A third prudential indicator is the Liability Benchmark (LB). The Authority is required to estimate and measure the LB for the forthcoming financial year and the following two financial years, as a minimum but CIPFA strongly recommend that the LB is produced for at least 10 years or covering the full debt maturity profile.

There are four components to the LB: -

1. **Existing loan debt outstanding**: the Authority's existing loans that are still outstanding in future years.
2. **Loans CFR**: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP.
3. **Net loans requirement**: this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned MRP and any other major cash flows forecast.
4. **Liability benchmark** (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance.

The Liability benchmark in the graph below (red dotted line) is a projection of our external borrowing requirement. External borrowing should rarely exceed the Liability Benchmark. Note: the Liability benchmark excludes finance leases.



5.4 Core funds and expected investment balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year-end balances for each resource and anticipated day to day cash flow balances.

Year End Resources £000	2023/24 Actual	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
Fund balances / reserves	16,515	7,658	7,188	6,650	6,150
Provisions	782	500	500	500	500
Total core funds	**17,297**	**8,158**	**7,688**	**7,150**	**6,650**
Working capital*	7.406	7,250	7,000	5,000	5,000
Total cash to invest	**24,703**	**15,408**	**14,688**	**12,150**	**11,650**
(Under)/over borrowing	**(20,231)**	**(14,193)**	**(13,475)**	**(10,803)**	**(10,599)**
Expected external investments	**4,472**	**1,215**	**1,213**	**1,347**	**1,051**

5.5 Affordability Prudential Indicator

This prudential indicator is required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicator:

Ratio of financing costs to net revenue stream. This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

%	2023/24 Actual	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
General Fund	3.35	7.97	11.91	13.83	15.95

The estimates of financing costs include current commitments and the proposals in this budget report.

5.6 Minimum revenue provision (MRP) policy statement

Under Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, where the Authority has financed capital expenditure by borrowing it is required to make a provision each year through a revenue charge (MRP).

The Authority is required to calculate a prudent provision of MRP which ensures that the outstanding debt liability is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The MRP Guidance (2024) gives four ready-made options for calculating MRP. An authority can use a mix of these options, or the authority can use at alternative method if more appropriate to do so.

The MRP policy statement requires full council approval in advance of each financial year. The Council is recommended to approve the following MRP Statement:

From 1 April 2008 for all unsupported borrowing the MRP policy will be*:*

Asset Life Method (Straight line) – MRP will be based on the estimated life of the assets.

Regulation 27 (3) allows a local authority to charge MRP in the financial year following the one in which capital expenditure financed by debt was incurred.

Capital expenditure financed by borrowing 2024/25 will not be subject to an MRP charge until 2025/26, or in the financial year following the one which the asset first becomes available for use.

The Authority will apply the asset life method for any expenditure capitalised under a Capitalisation Direction.

MRP in respect of assets acquired under Finance Leases or PFI will be charged at an amount equal to the principal element of the annual repayment.

For capital expenditure on loans to third parties where the principal element of the loan is being repaid in annual instalments, the capital receipts arising from the principal loan repayments will be used to reduce the CFR instead of MRP.

Where no principal repayment is made in a given year, MRP will be charged at a rate in line with the life of the assets funded by the loan.

MRP Overpayments

Under the MRP guidance, any charges made in excess of the statutory MRP can be made, known as voluntary revenue provision (VRP).

VRP can be reclaimed in later years if deemed necessary or prudent. In order for these amounts to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year.

No VRP overpayments have been made to date.

6 Borrowing

The capital expenditure plans set out in Section 5, provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's Capital Strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of approporiate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the Annual Investment Strategy.

6.1 Current Portfolio Position

The overall treasury management cash portfolio as at 31 March 2024 and for the position as at 31st December 2024 are shown below for both borrowing and investments.

Treasury Portfolio **£000**	**31/03/24** **Actual**	**31/12/24** **Actual**
Investment with banks	4,472	8,900
Total investments managed in-house	**4,472**	**8,900**
Borrowing with PWLB	3,000	3,000
Borrowing with Local Authorities	0	3,000
Total external borrowing	**3,000**	**6,000**
Net treasury investments / (borrowing)	1,472	2,900

The Council's forward projections for borrowing are summarised below. The table shows the actual external debt, against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£000	2023/24 Actual	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
External Debt					
External borrowing at **1 April**	3,000	3,000	15,000	22,000	24,000
Expected change in external borrowing	0	12,000	7,000	2,000	0
Other long-term liabilities (finance leases) at **1 April**	1,337	2,813	5,356	5,074	5,300
Expected change in OLTL (finance leases)	1,476	2,543	(282)	226	(279)
Actual gross debt at 31 March	**5,813**	**20,356**	**27,074**	**29,300**	**29,021**
The Capital Financing Requirement	**26,044**	**34,549**	**40,549**	**40,103**	**39,620**
(Under) / over borrowing	**(20,231)**	**(14,193)**	**(13,475)**	**(10,803)**	**(10,599)**

Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2025/26 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes.

The Chief Financial Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

6.2 Treasury Indicators: limits to borrowing activity

The operational boundary. This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

Operational boundary £000	**2024/25 Estimate**	**2025/26 Estimate**	**2026/27 Estimate**	**2027/28 Estimate**
Debt	15,000	22,000	24,000	24,000
Other long term liabilities	6,500	6,500	6,500	6,500
Total	**21,500**	**28,500**	**30,500**	**30,500**

The Boundary is increasing to reflect the higher CFR and borrowing need over this period.

The authorised limit for external debt. This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.
2. The Council is asked to approve the following authorised limit:

Authorised limit £000	**2024/25 Estimate**	**2025/26 Estimate**	**2026/27 Estimate**	**2027/28 Estimate**
Debt	33,000	35,000	35,000	35,000
Other long term liabilities	7,500	7,500	7,500	7,500
Total	**40,500**	**42,500**	**42,500**	**42,500**

IFRS 16 – Leasing

IFRS 16 is a change of accounting model for leases over 12 months, with implementation in the 2024/25 statement of accounts. This may bring more leased assests onto the balance sheet in a similar way to the vehicle fleet, showing as other long term liabilities. We are reviewing the impact of these changes and we will report back to Members once this work has been completed. This strategy has made an adjustment to the authorised limit for long term liabilities to allow some headroom for these changes.

6.3 Prospects for Interest Rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Link provided the following forecasts on 11th November 2024. These are forecasts for Bank Rate, PWLB certainty rates, gilt yields plus 80 bps.

Link Group Interest Rate View	11.11.24												
	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
BANK RATE	4.75	4.50	4.25	4.00	4.00	3.75	3.75	3.75	3.50	3.50	3.50	3.50	3.50
3 month ave earnings	4.70	4.50	4.30	4.00	4.00	4.00	3.80	3.80	3.80	3.50	3.50	3.50	3.50
6 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
12 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
5 yr PWLB	5.00	4.90	4.80	4.60	4.50	4.50	4.40	4.30	4.20	4.10	4.00	4.00	3.90
10 yr PWLB	5.30	5.10	5.00	4.80	4.80	4.70	4.50	4.50	4.40	4.30	4.20	4.20	4.10
25 yr PWLB	5.60	5.50	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.50
50 yr PWLB	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.40	4.30	4.30

Additional notes by Link on this forecast table: -

- *Following the 30 October Budget, the outcome of the US Presidential election on 6 November, and the 25bps Bank Rate cut undertaken by the Monetary Policy Committee (MPC) on 7 November, we have significantly revised our central forecasts for the first time since May. In summary, our Bank Rate forecast is now 50bps – 75bps higher than was previously the case, whilst our PWLB forecasts have been materially lifted to not only reflect our increased concerns around the future path of inflation, but also the increased level of Government borrowing over the term of the current Parliament.*

- *Our central view is that monetary policy is sufficiently tight at present to cater for some further moderate loosening, the extent of which, however, will continue to be data dependent. We forecast the next reduction in Bank Rate to be made in February and for a pattern to evolve whereby rate cuts are made quarterly and in keeping with the release of the Bank's Quarterly Monetary Policy Reports (February, May, August and November).*

- *Regarding our PWLB forecast, the short to medium part of the curve is forecast to remain elevated over the course of the next year, and the degree to which rates moderate will be tied to the arguments for further Bank Rate loosening or otherwise. The longer part of the curve will also be impacted by inflation factors, but there is also the additional concern that with other major developed economies such as the US and France looking to run large budget deficits there could be a glut of government debt issuance that investors will* *only agree to digest if the interest rates paid provide sufficient reward for that scenario.*

Gilt yields and PWLB rates

The overall longer-run trend is for gilt yields and PWLB rates to fall back over the timeline of our forecasts, but the risks to our forecasts are to the upsides. Our target borrowing rates are set two years forward (as we expect rates to fall back) and the current PWLB (certainty) borrowing rates are set out below: -

PWLB debt	Current borrowing rate as at 11.11.24 p.m.	Target borrowing rate now (end of Q3 2026)	Target borrowing rate previous (end of Q3 2026)
5 years	5.02%	4.30%	3.90%
10 years	5.23%	4.50%	4.10%
25 years	5.66%	4.90%	4.40%
50 years	5.42%	4.70%	4.20%

Borrowing advice: *Our long-term (beyond 10 years) forecast for Bank Rate has been increased to 3.25% (from 3%). As all PWLB certainty rates are currently significantly above this level, borrowing strategies will need to be reviewed in that context. Overall, better value can be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should also be considered. Temporary borrowing rates will, generally, fall in line with Bank Rate cuts.*

6.4 Borrowing Strategy

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council’s reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as medium and longer dated borrowing rates are expected to fall from their current levels, albeit only once prevailing inflation concerns are addressed by restrictive near-term monetary policy. That is, Bank Rate remains elevated in 2025 even if some rate cuts arise.

Against this background and the risks within the economic forecast, caution will be adopted with the 2025/26 treasury operations. The Chief Financial Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in borrowing rates,* then borrowing will be postponed.
- *if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.*

Any decisions will be reported to the Leader and Lead Member for Resources and Commercialisation.

Significant capital investment over recent financial years, for schemes such as new Leisure Centre and the purchase of Green Lanes Shopping Centre resulted in a Capital Financing Requirement (CFR) brought forward balance for 24/25 of circa £23m, excluding finance leases. Further unfinanced capital expenditure during the year on our recycling centre and the Future High Street project will increase the projected CFR to circa £29m as at 31st March 2025.

As at 31st December 2024, this capital spend had largely been supported by internal borrowing with £3m of external borrowing from the PWLB and a further £3m of short term borrowing from another Local Authority.

However during January 2025, based on our cash flow projections, we have taken on a further £2m of borrowing from the PWLB. Therefore total external borrowing currently stands at £8m at 31st January 2025. We anticipate to borrow up to a further £7m this financial year, which would see external borrowing potentially total £15m as at 31st March 2025.

Looking ahead to 2025/26, the approved capital programme has an additional borrowing need of £7m to complete the Future High Street Project and associated works and improvements at Green Lanes. Our external borrowing is also projected to increase by £7m to £22m in total. This still assumes that our own cashflow and resources can cover circa £13m of internal borrowing.

Members should note that any slippages to the capital programme expenditure and/or additional capital receipts or grants received would reduce the amount of actual borrowing undertaken. Likewise any increased capital expenditure, approved in year, may result in the need for additional borrowing.

Given the interest rate forecasts, borrowing will be kept short term so that the Council can benefit from lower borrowing rates on maturity.

The graph below sets out the current borrowing strategy for the next ten years. For further details please refer to the Council's ten year capital strategy on this agenda.

6.5 Maturity structure of borrowing

These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Council is asked to approve the following treasury indicators and limits:

Maturity Structure of fixed interest rate borrowing 2025/26		
	Lower	**Upper**
Under 12 months	0%	90%
12 months to 2 years	0%	90%
2 years to 5 years	0%	100%
5 years to 10 years	0%	100%
10 years and above	0%	90%
Maturity Structure of variable interest rate borrowing 2025/26		

	Lower	Upper
Under 12 months	0%	90%
12 months to 2 years	0%	90%
2 years to 5 years	0%	100%
5 years to 10 years	0%	100%
10 years and above	0%	90%

6.6 Control of interest rate exposures

The Council is asked to approve the following local indicator to reduce the impact of any adverse movement in interest rates, whilst not impairing opportunities to reduce costs / improve performance.

Interest rate Exposures	2025/26	2026/27	2027/28
Limit on fixed interest rates:			
• **Debt only**	100%	100%	100%
• **Investments only**	100%	100%	100%
Limit on variable interest rates:			
• **Debt only**	30%	30%	30%
• **Investments only**	100%	100%	100%

Paragraphs 6.3, 6.4, 6.5 and 7.4 provide further details on the controls in place to limit and manage interest rate exposure in line with financial requirements, borrowing maturities and interest rate forecasts.

6.7 Policy on borrowing in advance of need

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid year or annual reporting mechanism.

6.8 Debt rescheduling

Rescheduling of current borrowing in our debt portfolio may be considered whilst premature redemption rates remain elevated but only if there is surplus cash available to facilitate any repayment, or rebalancing of the portfolio to provide more certainty is considered appropriate.

If rescheduling is to be undertaken, it will be reported to the Leader and Lead Member for Resources and Commercialisation.

6.9 New financial institutions as a source of borrowing and / or types of borrowing

Currently the PWLB Certainty Rate is set at gilts + 80 basis points. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons:

- Local authorities (primarily shorter dated maturities out to 3 years or so – generally still cheaper than the Certainty Rate)
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates)
- UK Municipal Bonds Agency and UK National Wealth Fund, if appropriate

Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.

Given the relative scale of our external borrowing it is likely that the PWLB will remain the Council's best option as a source of borrowing.

6.10 Approved Sources of Long and Short term Borrowing

Members are asked to review and approve the following list of sources and types of funding:

On Balance Sheet	**Fixed**	**Variable**
PWLB	●	●
UK Municipal Bond Agency	●	●
Local Authorities	●	●
Banks	●	●
Pension Funds	●	●
Insurance Companies	●	●
UK National Wealth Fund	●	●
Market (long-term)	●	●
Market (temporary)	●	●
Market (LOBOs)	●	●
Stock issues	●	●
Local temporary	●	●
Local Bonds	●	
Local Authority Bills	●	●
Overdraft		●
Negotiable Bonds	●	●
Internal (capital receipts & revenue balances)	●	●
Commercial Paper	●	
Medium Term Notes	●	
Finance leases	●	●

7 Annual Investment Strategy

7.1 Investment Policy – management of risk

The Ministry of Housing, Communities and Local Government (MHCLG) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This section deals solely with treasury (financial) investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets and service investments, are covered in section 8 only and in the Capital Strategy (a separate report).

The Council's investment policy has regard to the following: -

- MHCLG's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 ("the Code")
- CIPFA Treasury Management Guidance Notes 2021

The Council's investment priorities will be security first, portfolio liquidity second and then yield, (return). The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's low risk appetite.

In the current economic climate, it is considered appropriate to maintain a degree of liquidity to cover cash flow needs but to also consider "laddering" investments for periods up to 12 months with high credit rated financial institutions, whilst investment rates remain elevated.

The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

1. Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

2. **Other information**: ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as "**credit default swaps**" and overlay that information on top of the credit ratings.

3. **Other information sources** used will include the financial press, share price and other such information pertaining to the financial sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

4. This authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. Appendix A list the instruments under the categories of ‘specified’ and ‘non-specified’ investments.

   - **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.
   - **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. The Council will consider using this category only for investments that would come under Specified, except that the maturities are greater than 1 year.

5. **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the matrix table in paragraph 7.2.

6. **Transaction limits** are set for each type of investment in paragraph 7.2.

7. This authority will set a limit for the amount of its investments which are invested for **longer than 365 days**, (see paragraph 7.4).

8. Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating**, (see paragraph 7.3).

9. This authority has engaged **external consultants**, (see paragraph 4.5), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

10. All investments will be denominated in **sterling**.

11. As a result of the change in accounting standards for 2023/24 under **IFRS 9**, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund.

However, this authority will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see paragraph 7.4). Regular monitoring of investment performance will be carried out during the year.

Changes in risk management policy from last year.

The above criteria is largely unchanged from last year.

7.2 Creditworthiness policy

This Council applies the creditworthiness service provided by the Link Group. This service employs a sophisticated modelling approach utlilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- "watches" and "outlooks" from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, watches and outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads. The end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands*:*

- Dark pink 5 years for Ultra-Short Dated Bond Fund with a credit score of 1.25
- Light pink 5 years for Ultra-Short Dated Bond Fund with a credit score of 1.5
- Yellow 5 years (UK Government debt)
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi-nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days

- No Colour not to be used

The Link creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council use will be a short term rating (Fitch or equivalents) of F1 and a long term rating A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored weekly. The Council is alerted to changes to ratings of all three agencies through its use of the Link creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swap spreads against the iTraxx Eurpoean Senior Financials benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on any external support for banks to help support its decision making process.

	Colour (and long term rating where applicable)	Money Limit	Time Limit
Banks	**yellow**	**£1m**	**5 yrs**
Banks	**purple**	**£1m**	**2 yrs**
Banks	**orange**	**£4m**	**1 yr**
Banks – part nationalised	**blue**	**£4m**	**1 yr**

Banks	**red**	**£3.5m**	**6 mths**
Banks	**green**	**£3.5m**	**100 days**
Banks	**No colour**	**Not to be used**	
Other institutions limit	**-**	**£2m**	**1yr**
DMADF	**UK sovereign rating**	**Unlimited**	**6 months**
Local authorities	**n/a**	**£3m**	**1yr**
	Fund rating*	**Money Limit**	**Time Limit**
Money market funds CNAV	**AAA**	**£3m**	**liquid**
Money market funds LVNAV	**AAA**	**£3m**	**liquid**
Money market funds VNAV	**AAA**	**£3m**	**liquid**
Ultra-Short Dated Bond Fund with a credit score of 1.25	**Dark pink / AAA**	**£1m**	**liquid**
Ultra-Short Dated Bond Fund with a credit score of 1.5	**Light pink / AAA**	**£1m**	**liquid**

- *fund ratings are different to individual counterparty ratings, coming under either specific MMF or Bond Fund rating criteria*

No limit will be set on placing funds with the Council's own bank due to the volatility / fluctuations in day to day cash flows. Should the Council's bank have no colour then funds will be kept instant access.

Group limits where a number of institutions are under one ownership is a maximum of £6m.

Creditworthiness

Significant levels of downgrades to Short- and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. Nonetheless, when setting minimum sovereign debt ratings, this Authority will not set a minimum rating for the UK

7.3 Country limits

The Council has determined that it will mainly use approved counterparties from within the United Kingdom.

However, the Council may consider counterparties from outside the United Kingdom providing the country has a minimum sovereign credit rating of AA- from Fitch or equivalent.

7.4 Investment Strategy

In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. The current shape of the yield curve suggests that the risks are relatively balanced between Bank Rate staying higher for longer, if inflation picks up markedly through 2025 post the 30 October 2024 Budget, or it may be cut quicker than expected if the economy stagnates. The economy only grew 0.1% in Q3 2024, but the CPI measure of inflation is now markedly above the 2% target rate set by the Bank of England's Monetary Policy Committee two to three years forward.

While most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

Investment returns expectations.

The current forecast shown in section 6.3, includes a forecast for Bank Rate to fall to a low of 3.5%.

The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows:

Average earnings in each year	
2024/25 (residual)	4.60%
2025/26	4.10%
2026/27	3.70%
2027/28	3.50%
2028/29	3.50%
Years 6 to 10	3.50%
Years 10+	3.50%

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access, notice accounts and short-dated deposits, (overnight to 100 days), in order to benefit from the compounding of interest.

Investment treasury indicator and limit - total principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Council is asked to approve the treasury indicator and limit: -

Upper limit for principal sums invested for longer than 365 days			
£m	**2025/26**	**2026/27**	**2027/28**
Principal sums invested for longer than 365 days	£1m	£1m	£1m

The Council currently has no investments in excess of one year.

Investment risk benchmarking.

This Council will use an investment benchmark to assess the investment performance of its investment portfolio of 7 day SONIA compounded rate. (Sterling Overnight Index Average which is the risk-free rate for sterling markets administered by the Bank of England)

The Chief Financial Officer will monitor the current and trend position of the treasury function and amend the operational strategy to manage risk, as interest rates and counterparty conditions change. Performance results will be reported through the Quarterly Performance and Financial Management, Mid-Year and Annual Treasury reports to Strategy and Resources Committee.

8 Non-Treasury Investments

The PWLB will no longer lend to local authorities that plan to buy commercial assets primarily for yield. Therefore the Council will not undertake any such commercial investments within this context.

The Council will consider service investments that relate to a specific council objectives approved directly though a committee, such as schemes in relation to economic regeneration. Service investment items are covered by the capital programme and associated risk framework rather than non-treasury practices.

9 Resource Implications

9.1 As detailed in the report.

10 Equalities Assessment

10.1 There are not any equalities implications anticipated as a result of this report, as the purpose of this report is to present the Council's financial position only.

11 Environmental Assessment

11.1 The Council will consider approved Counterparties that provide an environmental, social and governance (ESG) alternative i.e. sustainable deposits, which help to support sustainable and environmentally friendly services and products, whilst delivering Security, Liquidity and Yield requirements. This approach complies with the current Secretary of State Investment Guidance and ensures no greater risk is taken to achieve ESG/Sustainable investment objectives.

11.2 This Council will maintain a cautious approach to ESG investments and will work with our external Treasury Advisors to help understand and evaluate the risk involved.

12 Corporate Priorities

12.1 The Treasury management function supports the delivery of the Councils capital programme and ensures cash flows meets the day to day requirements for service delivery.

13 Constitutional context

Part 3 Annexe 1, para 1(c) – delegated power

Article 4.5.26 and Part 4 (Financial Procedure Rules) para 13.8 - referred power

14 Statement of Confidentiality

14.1 This report contains no confidential or exempt information under the provisions of Schedule 12A of 1972 Act.

15 Statement of Internal Advice

15.1 The author (below) confirms that advice has been taken from all appropriate Councillors and Officers.

Adam Tape, Head of Governance
Jon Triggs, Director of Resources and Deputy Chief Executive